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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1947

THE AVIATION CLUB OF UTAH, a corporation,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

MAY IT PLEASE THE COURT:

Your petitioner, The Aviation Club of Utah, a corporation, petitions this Honorable Court for a writ of certiorari to review a judgment of the United States Circuit Court of Appeals for the Tenth Circuit in the above entitled case. Petitioner respectfully represents to this court:

SUMMARY STATEMENT OF MATTER INVOLVED

From its operations as a private social club, The Aviation Club of Utah had revenues and net earnings in the years 1941, 1942 and 1943. It claims that all of those revenues were and are exempt from income, declared value excess profits, and excess profits taxes by Section 101 (9) of the Internal Revenue Code which reads:

> **"101. Exemptions from tax on corporations.**
> The following organizations shall be exempt from taxation under this chapter—
>
> (9) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes,

no part of the net earnings of which inures to the benefit of any private shareholder.'"

Specifically, your petitioner contends that it is a private club organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, and that no part of its net earnings inured to the benefit of any private shareholder. Its contention in those particulars was rejected by the defendant Commissioner of Internal Revenue. The case was then submitted to the Tax Court of the United States.

The Tax Court ruled that the exemption claimed by your petitioner applied to earnings for 1941 but not to the earnings of 1942 and 1943, and, therefore, sustained the taxes levied for those two years. (R 27, 28) Upon review the Circuit Court of Appeals for the Tenth Circuit affirmed the decision of the Tax Court. (R 151)

Petitioner was organized in 1940 for social, recreational and other nonprofitable purposes in accordance with applicable provisions of the corporation code of Utah. It has never issued any capital stock and membership is not assignable, either by a member or by operation of law. (R 18) In 1941 the club, by contract of purchase, acquired possession of a clubhouse in the residential section of Salt

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[1]Helpful in connection with the sections of the revenue law involved is the first paragraph of the Tax Court's opinion. R. 24:

"The petitioner claims exemption from tax under section 101 (9), I. R. C. That section provides that 'Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private stockholder' shall be exempt from taxation under Chapter 1. The income tax is imposed by Chapter 1, but the declared value excess profits and the excess profits tax are imposed by Chapter 2. Section 727 (a) provides that corporations exempt under section 101 from the tax imposed by Chapter 1 shall be exempt from tax imposed by Subchapter E-Excess Profits Tax. The declared value excess profits tax is imposed under Subchapter B of Chapter 2. Section 600 provides that if any corporation is taxable under section 1200, a declared value excess profits tax shall be imposed. Section 603 provides that all provisions of law applicable in respect of taxes imposed by Chapter 1 shall, in so far as not inconsistent with Subchapter B, be applicable in respect of the declared value excess profits tax. The petitioner does not contest the additions to the tax for delinquency in filing returns except by its single contention that it was wholly exempt from tax for all three years."

Lake City. Its clubhouse has none of the appearances of a commercial or public institution and no advertising of any kind whatsoever has been resorted to to indicate to the passerby the existence of the club as such. (R 18)

The only testimony upon the subject indicates that the purpose of the club was entirely nonprofit. (R 18) Its organization resulted from a desire on the part of the organizers (thirty individuals who had a common interest in aviation) to provide a place of relaxation and association for those interested in aviation. Impetus was given to the organization and development of the club by General Ralph Royce, who commanded a small contingent of Air Corps officers in or near Salt Lake City prior to Pearl Harbor, and who hoped for the creation of a place where his flyers might find social relaxation and companionship. (R 41)

It was the design of the organizers that nonresident friends might become guest or associate members temporarily and thereby find pleasure and recreation in the club rooms. (R 45) As early as 1941, military installations in and near Salt Lake City began to multiply and the number of military officers in Salt Lake City who were seeking recreation such as the club furnished greatly increased. (R 80, 94) The U. S. O. was set up to care for the needs of enlisted men, but there was no equivalent for officer personnel stationed temporarily in or near Salt Lake City. (R 90, 91) Commanding officers of military installations and executives of the civilian defense urged upon all private clubs the necessity of making available their accommodations for the entertainment of officer personnel. It was thought that such was both necessary and desirable in the interest of morale. (R 89-91) The extension by your petitioner of its hospitality to a rapidly increasing number of officers did not result from any design to commercialize their presence in this community. Your petitioner became a victim of circumstances. It responded patriotically to a patriotic appeal or demand that all such places be devoted in so far as they could to the preservation and building of morale among officers. (R 26)

In the latter part of 1941 and the early part of 1942, many out-of-town officers were accepted by the club as guest

members and for the brief time they were stationed in the vicinity they exercised the privilege of associate members and received and paid for club accommodations on the same basis as regular members. (R 20, 57, 59, 46) In the spring of 1942 the Eighteenth Replacement Wing of the Army Air Force was established at Salt Lake City and the number of young officers seeking accommodations equivalent to those of your petitioner greatly multiplied and correspondingly increased the demand upon your petitioner for such services as it had. As the number of officers multiplied in and about Salt Lake City, the pressure from commanding officers upon your petitioner and others to contribute to the entertainment and recreation of officers grew. (R 20, 45, 89, 90)

Prior to the establishment of the Eighteenth Replacement Wing in Salt Lake City, officers became guest members of the club in substantial number, but the number who availed themselves of this privilege after the spring of 1942 was so far increased, that in 1942 and 1943 the number of such guest members and the amount of money paid into the club's revenues by them was much greater than before. There was, however, no differences in quality between the relationship of the club and army officers in 1941 and 1942. Only because of the increased demand from such men, the club adopted the principle of recognizing the uniform of the Army, Navy or Marine officer as sufficient to justify a man's acceptance as a guest member.

Shortly after V-J Day, the practice of extending guest privileges to military officers was stopped. (R 48) Your petitioner then received letters of thanks and appreciation from commanders whose men had been accorded the use of the club's facilities. (R 49)

The membership of the club consists of regular members who alone have the right to vote, and guest, or associate members, who have no right to vote but who otherwise have the right to enjoy all the privileges of the club at the same price charged regular members. The average number of regular members during 1941, 1942 and 1943, was 212, 162, and 154, respectively. The record does not show

the number of persons who enjoyed privileges as guest or associate members in 1941. In 1942 the number was somewhere between 3,000 and 4,500; and in 1943 somewhere between 9,000 and 10,000. (R 20)

While the Tax Court emphasizes the vast increase in the number of officers who became guest members in 1942 and 1943, nevertheless, the Tax Court found and held: *"The clubhouse was never opened to the public."* (R 20)

The clubhouse was never opened to the public in any of the three years under review. Many officers availed themselves of the accommodations of the club but they cannot be said to be "the public," as the Tax Court has made the finding that the club was never opened to the public. The only difference in the operation of the club in 1942 and 1943 as compared with 1941 is in the number of guest members accommodated and the amount of revenue resulting from their presence. The Tax Court did not point out, and the evidence would not support a finding that there is any other substantial difference between 1941 and either of the two years following.

The Tax Court not only found that the clubhouse was never opened to the public, but it also found that "the petitioner has never distributed any of its income or assets to its members." (R 22) Officers of the club as such were paid no compensation, either directly or indirectly.

When the club moved into its clubhouse it had neither funds with which to equip the place, nor experience with which to operate. It, therefore, entered upon a contract with a concessionaire who furnished the place and operated it for a time. He paid a rental and a percentage of the profits. When his contract terminated, the club purchased his equipment and inventory, and ever since that time has managed the club without his help. The concessionaire, during his tenure, was not a member of the club, but he was at all times subject to the direction of the Board of Directors as to the extent and cost of service and the method of managing the institution. (R 46, 47)

In addition to findings quoted above that, "none of the club's income or assets was ever distributed to any member as such," and "the clubhouse was never opened to the public," the Tax Court found with respect to the year 1941:

(a) "The petitioner, during 1941, was a club organized and operated exclusively for pleasure, recreation, and other non-profitable purposes, no part of the net earnings of which inured to the benefit of any private stockholder."

With respect to 1942 and 1943, the court found:

(b) "Its profits for 1942 from the use of the club and its services by nonmembers were several times as large as the amount of dues and profits received from the use of the club and its services by members.

(c) "Its profits for 1943 from the use of the club and its services by members were about ten times as large as the amount of dues and profits received from the use of the club and its services by members.

(d) "The profits for 1942 and those for 1943 received by the petitioner from the use of the club and its services by nonmembers inured to the benefit of its members.

(e) "The petitioner, during 1942 and 1943, was not a club organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inured to the benefit of its members." (R 23)

Paragraphs (a), (b), (c), (d), and (e) in the Tax Court's findings follow each other. (R 23) They show the logic of the decision of the Tax Court and the Circuit Court of Appeals. They point out that the only difference considered by the Tax Court between the years 1942 and 1943 on the one hand and the year 1941 on the other is in the volume and origin of the revenue.

In finding that the petitioner was covered by the statutory exemption in 1941, but not covered in 1942 or 1943, the

court below applied a quantitative standard to petitioner's revenues, which is not justified by the statute or the decided cases. In ruling that the revenues of the club in 1942 and 1943 inured to the benefit of shareholders, it adopted a rule which would effectively defeat the statutory exemption in the case of all social clubs except those in failing circumstances and having no earnings.

REASONS RELIED ON FOR ALLOWANCE OF WRIT

1. The correct interpretation and proper construction of an exemption statute which affects the revenues of all social clubs and nonprofit organizations throughout the country is a matter of such public interest and concern as to deserve a final settlement by this court.

2. It is of public importance that the following questions be answered with regard to revenues and earnings of clubs organized for social and nonprofitable purposes:

(a) Does the amount of the earnings of such a club determine whether earnings are exempt? If such a club has earnings, can it be said that they inure to the benefit of the members because the financial condition of the organization is thereby improved?

3. The decision of the Tenth Circuit Court of Appeals rendered in this case is probably in conflict with applicable decisions of this court and is also in conflict with decisions of other Circuit Courts of Appeal on the same question.

WHEREFORE, your petitioner prays that a writ of certiorari issue under the seal of this court to the United States Circuit Court of Appeals for the Tenth Circuit, commanding said court to certify and send to this court a full and complete transcript of the record and of the proceedings of said court numbered and entitled on its docket No. 3465, The Aviation Club of Utah, a corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent, to the end that this cause may be reviewed and determined by this court as provided for by the statutes of the United States; and that the judgment herein of said United States Circuit

Court of Appeals for the Tenth Circuit be reversed by this court, and for such other and further relief as to this court may seem proper.

Dated this 24th day of October, 1947.

PAUL H. RAY
S. J. QUINNEY
Attorneys for Petitioner.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

I.

OPINIONS OF THE COURT BELOW

Opinion of the Circuit Court of Appeals for the Tenth Circuit dated June 30, 1947, will be found R. 151 and is reported in 162 F. (2d) 984. Decision of United States Tax Court will be found R. 17-27.

II.

JURISDICTION

1. The date of the judgment to be reviewed is June 30, 1947. An order of this court granting sixty days additional time within which to file petition for certiorari is dated September 26, 1947, and is on file with the Clerk of this Court. The jurisdiction of this court is invoked under U. S. C. A. Title 26, Sec. 1141.

2. The decision of the lower court involves the interpretation of Sub-section 9, Section 101 of the Internal Revenue Code, which exempts from income taxes and some related taxes the revenues of clubs organized and operated exclusively for pleasure, recreation and other nonpofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder. Petitioner claimed that its revenue for 1941, 1942 and 1943 were exempt under that

section. The Tax Court and the Circuit Court of Appeals ruled that the exemption did not apply to 1942 and 1943, but was applicable to 1941. The decision of the Tax Court and of the Circuit Court of Appeals was based upon the finding of the Tax Court that that portion of the revenues of the club for 1942 and 1943 derived from guest members was disproportionately greater than the portion derived from dues and revenues otherwise derived from regular members. (R 23) The Tax Court found, and the Tenth Circuit Court of Appeals affirmed, that the revenues of the club inured to the benefit of the members.

3. The decision of the court below affirming the decision of the Tax Court is probably in conflict with *Trinidad v. Sagrada*, 263 U. S. 578, 68 L. Ed. 458.

4. The decision of the court below affirming the decision of the Tax Court is in conflict with *Scofield v. Corpus Christi Golf Club*, 127 F. (2d) 452; *Santee Club v. White*, 87 F. (2d) 5; *Roche's Beach, Inc. v. Commissioner*, 96 F. (2d) 776; *Koon Kreek Klub v. Thomas*, 108 F. (2d) 616; *Debs Memorial Radio Fund v. Commissioner*, 148 F. (2d) 948; *Anderson Country Club v. Commissioner*, 2 T. C. 1238.

5. The public interest will be promoted by a decision of this court settling the question when, if at all, and under what conditions a club organized for purely social and non-profit purposes may lose the tax exemptions provided by 101 (9) of the Internal Revenue Code.

III.

STATEMENT OF THE CASE

The case is briefly stated in preceding petition for certiorari.

IV.

SPECIFICATION OF ERRORS

1. The Circuit Court of Appeals for the Tenth Circuit erred in affirming the Tax Court and holding that petitioner's earnings for 1942 were not exempt under 101 (9).

2. The Circuit Court of Appeals for the Tenth Circuit erred in affirming the Tax Court and holding that petitioner's earnings for 1943 were not exempt under 101 (9).

3. The Circuit Court of Appeals for the Tenth Circuit erred in holding that revenues for 1942 inured to the benefit of any shareholder.

4. The Circuit Court of Appeals for the Tenth Circuit erred in holding that revenues for 1943 inured to the benefit of any shareholder.

5. The Circuit Court of Appeals for the Tenth Circuit erred in approving the application of a quantitative and origin test to petitioner's earnings to determine whether they were exempt.

V.
ARGUMENT

SUMMARY

The statutory exemption relied upon by petitioner exempts clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder.

That petitioner is a club, and that it was organized exclusively for pleasure, recreation and other nonprofitable purposes, is not denied. Such was the finding of the Tax Court and that finding was not disturbed by the Circuit Court of Appeals.

The Tax Court and the Circuit Court of Appeals concluded that after 1941 petitioner departed from the purposes for which it was organized; that it thereafter operated for profit and that its earnings inured to the benefit of its shareholders. The revenues and earnings of the club did increase in 1942 over 1941 and in 1943 over 1942, but the conclusion that in either year the club had departed from the purposes for which it was organized or that its earnings inured to the benefit of its shareholders is contrary to the exemption statute and in conflict with decisions of this court and of other circuit courts of appeal.

Earnings of petitioner in 1942 and 1943 were condemned by the courts below as nonexempt, because they were larger than those of 1941 and because they *originated* more with commissioned officers who were guest members than with regular members. That condemnation required the application of quantity and origin of income as a standard for determining whether the exemption applied. Such standards are not embraced in either statute or lawful regulation and are disapproved by applicable decisions.

The conclusion that the earnings of 1942 and 1943 inured to the benefit of private shareholders is based upon the findings that such earnings permitted petitioner to keep up the installments on its clubhouse, to purchase some unimproved adjoining ground for purely club purposes and to set aside a fund for postwar betterment of the club's facilities. Such a conclusion is unsound; is unsupported by any applicable decision and would destroy the exemption in the case of any social club which operated at a profit.

DETAIL OF ARGUMENT

Petitioner had been in existence only a little more than a year when war came and it, like all others, found itself existing under new and strange conditions. Petitioner began existence according to the familiar pattern of social clubs. In June of 1941 it made a down payment on a clubhouse and moved in. It had regular members and associate or guest members. It had a few rooms to rent, a library, a buffet and a dining room.

As war approached Army personnel filtered into Salt Lake City. Among them were some flying officers under command of General Ralph C. Royce. General Royce encouraged petitioner to accept his flyers into its hospitality so that they might have the freedom of refined and private surroundings.

Petitioner accommodated such officers within the limits of its capacity, but no change was ever made in petioner's organization and its purpose to own and maintain a private, nonprofit club was never abandoned.

As time passed and war came on the number of commissioned officers in and about Salt Lake City increased and in the spring of 1942 the Eighteenth Replacement Wing was established nearby. Hundreds of flying officers came to that base to stay a few days and then be gone to be replaced by others.

Petitioner had arranged to accommodate the smaller number of officers in 1941 and was urged by military commanders and civilian leaders alike to extend hospitality to ever increasing numbers. (R 80, 90, 91) In response to such importunings, petitioner accepted as guest members as many officers as it could accommodate. Because of the overwhelming influx of Army personnel, petitioner was almost helpless in the matter.

The number of officers applying was so great and their stay in Salt Lake was so short it was not feasible to charge them either dues or initiation fees. (R 46) The time came in 1942 when the uniform of an officer of the United States was regarded as sufficient credentials to justify the wearer's acceptance as a guest member. If such a one applied he was given a book of rules to govern his conduct and was permitted to enjoy the services of the club at the price charged regular members.

Officers so accommodated spent money with the club and increased its earnings. But, as found by the Tax Court, "the club was never opened to the public." While the war lasted it would have been quite impossible for petitioner to gracefully turn officers from its doors. But as soon as hostilities ceased guest privileges were withdrawn. This was inconsistent with the idea that the club's purposes had become commercial as earnings could have been kept at a high level by continued acceptance of officers as guest members on the basis of the earlier years.

In *Trinidad v. Sagrada*, 263 U. S. 578, 68 L. Ed. 458, this court had before it the claim of a corporation sole of the Philippine Islands that it was organized and operated exclusively for religious, charitable and educational purposes and that no part of its net income inured to the bene-

fit of any shareholder or individual. Upon that claim it sought to recover income taxes which it had paid on account of profits derived from its operations. The company enjoyed large revenues from rents upon real estate, dividends upon securities, interest upon invested capital and substantial revenue from the sale of wine and chocolate. All of the profit realized by the corporation was spent or held and used for carrying on religious, charitable and educational work. In sustaining the claim of exemption from taxation and adjudging the corporation entitled to recover, this court observed in part:

> "Two matters apparent on the face of the clause go far towards settling its meaning. First, it recognizes that a corporation may be organized and operated exclusively for religious, charitable, scientific, or educational purposes, and yet have a net income. Next, it says nothing about the source of the income, but makes the destination the ultimate test of exemption."

The foregoing would seem to condemn the application of the origin or amount of revenue as the standard for determining whether the exemption applies. Circuit Courts of Appeal have so construed this Court's ruling in the *Sagrada* case. The effect of the *Sagrada* case cannot be avoided by stating that no such standard was applied in the case now under review as the findings of the Tax Court quoted earlier in this petition and brief at page 6 make it plain that such a standard was applied.

The Koon Kreek Klub was a hunting club. In the year involved it rented pasture for $500.00 and received a bonus of $25,000.00 for signing an oil lease covering a portion of its lands. The money so acquired was used to pay off a mortgage upon the property and for certain other purposes. The Circuit Court of Appeals for the Fifth Circuit ruled that the income of the club, including that from the pasture rental and oil lease was exempt, notwithstanding it had been used to free the club of indebtedness. *Koon Kreek Klub v. Thomas,* 108 F. (2d) 616.

The Santee Club owned a large fishing and hunting preserve. It sold a portion of its land at a profit. The Circuit Court of Appeals for the First Circuit ruled that the earn-

ings arising from the sale of the land were exempt. *Santee Club v. White,* 87 F. (2d) 5.

The Corpus Christi Golf and Country Club leased its golf course for oil drilling, for which it received a bonus and certain royalties. The use of the club for golf playing was somewhat interfered with by drilling operations, but was not suspended, notwithstanding the presence of oil derricks, etc. The interference was temporary and non-recurrent. The Fifth Circuit Court of Appeals ruled that the club had not lost its exemption. *Scofield v. Corpus Christ Golf and Country Club,* 127 F. (2d) 452. (5th C. C. A.)

In the court below the defendant Commissioner recognized the *Corpus Christi* case as against him but criticized the logic of the decision. We have then, at least by tacit admission, a clear conflict in the decision of the court below of which we seek review and the decision of the Fifth Circuit Court of Appeals in the *Corpus Christi* case.

The three cases just mentioned all involved Section 101 (9), the section relied upon by petitioner.

In *Debs Memorial Radio Fund v. Commissioner of Internal Revenue,* 148 F. (2d) 948, the Second Circuit Court of Appeals had before it Section 101 (8), a companion provision to 101 (9). It appears that the Radio Fund there involved was created to assist in advancing the views of socialism. It sold commercial time on its radio station in competition with purely commercial broadcasting companies and was seeking to increase the sale of commercial time. Profits were made but not distributed to any shareholder. The court ruled that notwithstanding the fund realized a large income from the sale of commercial time, its earnings were exempt.

Roche's Beach, Inc., was organized for the purpose of creating a medium through which a charitable foundation might come into funds to be used for charitable purposes. The income of the Beach arose from the sale of concessions for restaurants, refreshment stands, etc., from the rental of bathing suits, bathhouses and towels, and from the rental of certain houses located upon the beach. Notwithstanding

all the revenues came from what would otherwise be commercial operations, the Second Circuit Court of Appeals held that inasmuch as the profits were devoted to charitable purposes, the exemption applied. *Roche's Beach, Inc. v. Commissioner of Internal Revenue*, 96 F. (2d) 776, (C. C. A. 2nd.)

In all of the foregoing cases the Circuit Courts of Appeal followed the lead of this court in the *Sagrada* case. All of the revenues derived by your petitioner from its operations in 1942 and 1943 were either spent for or held by the club to be used exclusively for the purposes for which the club was organized: Social, nonprofit purposes.

The court below and the Tax Court ruled against petitioner upon authority of *West Side Tennis Club v. Commissioner*, 111 F. (2d) 6, and *Jockey Club v. Helvering*, 76 F. (2d) 597. We believe that those two cases clearly distinguish themselves from the case which we are here presenting. The West Side Tennis Club was for many years a club organized and operated in accordance with the requirements of the exemption statute. The time came, however, when it built a stadium with a seating capacity of more than 12,000 persons. The stadium was built at great expense for the sole purpose of accommodating such of the general public as might from year to year attend the national championship matches at Forest Hills. The stadium was to attract the public, not to give temporary and nonrecurring sanctuary to army officers in the clubhouse already acquired and in operation. The Tennis Club not only built the stadium to attract the public, but it did so in reliance upon the hope that attendance would recur year after year indefinitely. In arriving at its conclusion in the Tennis case, the court had before it *Santee Club against White*, supra, *Koon Kreek Klub v. Thomas*, supra, and *Trinidad v. Sagrada*, supra. It held that the situation of the Tennis Club was unlike that in any of the cases cited and, therefore, distinguishable. *Jockey Club v. Helvering*, supra, is clearly in the same class as the West Side Tennis case.

In *Coeur d'Alene Country Club v. Viley*, 64 F. Supp. 541, Judge Clark of the District of Idaho had before him

a claim arising under Section 101 (9) of the Revenue Code and reached a decision which we regard as in harmony with the contention we make here.

Notwithstanding the Tax Court found that the club never had any specific intention of distributing any of its profits to its members, the Circuit Court of Appeals for the Tenth Circuit concluded that the earnings and profits of the club for the years 1942 and 1943 inured to the benefit of the shareholders. The record shows without dispute that no property or assets of the club was ever distributed to any shareholder and no salary was ever paid to any officer of the club as such. One of the members of the club received a small salary for keeping the club's books of account, but no claim was ever made that the amount paid such person exceeded the value of his service. If it can be fairly held that the earnings of petitioner inured to the benefit of shareholders to the loss of the exemption provided by Section 101 (9), then it is doubtful that any club can ever enjoy the benefit of such exemption. Under such a ruling if a club has any net earnings, such earnings would inure to the benefit of the members and the exemption would be lost. In such view only if the club fails to have net earnings could it be said there is no benefit inuring to the members. Thus the exemption applies only to clubs which have no earnings and therefore no need of exemption. We must ascribe to Congress a different intention. If a social club starts operation with a debt, it must pay its debt or cease to operate. If it buys a clubhouse and makes a down payment, it must pay the balance or suffer foreclosure and dispossession. Every payment made on the purchase price reduces the danger of the foreclosure and improves the member's chance of continued enjoyment of his club. Final payment of the purchase price and creation of a surplus for maintenance, betterments and expansion promises added service and pleasure and enhances the value of membership. We suspect that such is the aim of every social club and such must have been in the mind of Congress. If such benefits deprive petitioner of statutory exemption, then what social club could be entitled to exemption?

In the court below, the Commissioner relied upon Section 29.101 (9)-1 of Regulation 111 and claimed that because the Regulation provides that when the club engages in traffic for profit, such club is not organized and operated exclusively for pleasure, etc. We deny that the Commissioner by regulation could to any extent repeal the exemption section, but in any event, all the claim for 29.101 (9)-1 of the regulation amounts to is that a standard related to quantity and origin of revenue is authorized by the statute. We reassert that the application of any such standard is contrary to the statute and to the applicable cases cited above.

If the Commissioner is right, then a club organized as petitioner was organized will begin each taxable year on an exempt status, but sometime during the year it may lose that exemption depending upon the quantity of its earnings. It will be at the mercy of the Commissioner or its agent, because it can look to no standard to determine when it has run past or outside of the coverage of the exemption.

Settlement of these questions seems to be of public importance. Wherefore, petitioner prays that its petition for certiorari be granted.

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Attorneys for Petitioner

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In the Supreme Court of the United States

OCTOBER TERM, 1947

No. 418

THE AVIATION CLUB OF UTAH, A CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 17–27) is reported at 7 T. C. 377. The opinion of the Circuit Court of Appeals (R. 151–155) is reported at 162 F. 2d 984.

JURISDICTION

The judgment of the Circuit Court of Appeals (R. 155) was entered on June 30, 1947. By order of this Court dated September 26, 1947, the time within which the petition for a writ of certiorari might be filed was extended for a period of 60 days from that date. (R. 157.) The petition for

a writ of certiorari was filed on October 30, 1947. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether or not the Club was exempt from taxation under Section 101 (9) of the Internal Revenue Code for the years 1942 and 1943.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved in this case are found in the Appendix, infra, pp. 14–18.

STATEMENT

The facts found[1] by the Tax Court (R. 18–23) may be summarized as follows:

The Club is a corporation, without capital stock, organized and existing under the laws of the State of Utah authorizing nonprofit corporations. It was organized on November 15, 1940, by 30 persons, living in or near Salt Lake City, who were interested in aviation. Each of the 30 original organizers loaned the Club $100 at that time for organization expenses and for the initial payment on a residence later purchased as a clubhouse. These loans were repaid by the Club in 1942. (R. 18.)

The purposes of the Club were the promotion of the interest of its members in aviation, the dis-

[1] Any reference to the evidence is made by specific record citation other than pages 18–23.

semination of information pertaining thereto and the providing of cultural, fraternal, social and educational activities for its members, particularly with respect to their interest in aviation. It had no intention to accumulate profits beyond the extent necessary for the Club's existence and no specific intention of distributing any of its profits to its members. Its articles of incorporation provided, however, that upon dissolution any surplus would be divided among the members then in good standing (R. 18) and a 1943 amendment provided that dissolution could take place at any time prior to its stated term of existence (R. 121).

The Club was originally composed of regular members elected by the nominating committee and the board of directors. They alone paid dues, were entitled to vote and hold office and to the privilege of inviting guests to the Club. The members totaled 162 during 1942 and 154 during 1943. The clubhouse was not open to the public. (R. 19–20.) Soon after the Club was organized it recognized "guest members" who were out-of-town friends or associates of regular members. Guest members paid for food and services at the Club at the same rate charged regular members. (R. 20.)

The clubhouse was acquired early in the summer of 1941 and since the Club had no funds with which to furnish it and no experience in the operation of a social club it entered into a con-

tract with one C. LeRoy Jensen to furnish and operate the Club. (R. 18–19.) Under this contract, made in April 1941, Jensen agreed to furnish and equip the clubhouse in exchange for the exclusive right to operate the dining room, a bar and other designated activities. He was to pay the Club a monthly rental and in addition the agreement provided that Jensen and the Club were to divide the profits from the operation of the concessions granted to Jensen. The percentage division of profits in effect from October, 1942, and for all of 1943 were graduated from 60–40 up to 80–20 to the Club. (R. 19.) Jensen was not at the time a member of the Club (R. 19), but his operations were under the direction of Club officials (R. 85–86). The agreement also provided that the Club could acquire the personal property placed in the clubhouse by Jensen and it did so in 1945 by the payment of $28,800 and thereafter operated the Club itself. (R. 19, 22.)

Early in 1942, at the request of Civilian Defense Authorities in Salt Lake City, who were seeking recreational facilities for the entertainment of officer service personnel temporarily in the city, the Club, actuated by patriotic motives, initiated the practice of issuing guest membership cards to male commissioned officers of the armed forces who presented themselves at the clubhouse and requested a card. These officers did not have to be sponsored by a club member. (R. 20.) In

1942 between 3,000 and 4,500 guest cards were issued to officers and between 9,000 and 10,000 during 1943. They had none of the usual prerogatives of membership and were required to pay in advance for all services furnished to them or to ladies accompanying them at the Club. The use of the Club by those officers was so great that regular members were materially restricted in their use of the Club during 1942 and 1943 (R. 20–21), and during those years the Club did not, because of that condition, seek to increase its regular membership (R. 22). The practice of issuing cards to commissioned service personnel was discontinued on VJ-Day. (R. 20.)

Jensen's gross receipts from the operation of the dining room, the bar and other facilities amounted to over $111,600 in 1942 and to more than $268,100 in 1943. (R. 21.) The Club received its share of these amounts. (R. 23.) In 1942 it purchased adjoining property for use as a parking lot and later it endeavored to pay off the balance of $12,493 remaining on its property but could not do so. (R. 22.) In 1943 or early in 1944 it made improvements to the tennis court and purchased for $1,000 an adjacent plot for a swimming pool. (R. 22.)

The Club filed blank returns for the taxable years 1941, 1942 and 1943, claiming exemption from taxes. (R. 18.) The Commissioner determined that the Club was not exempt under Section

101 (9) of the Internal Revenue Code; had net income of $20,750.12 in 1942 and $69,315.08 in 1943, and determined deficiencies (R. 22–23.) Because the returns were not filed within the time prescribed by law penalties were assessed. The deficiencies included income taxes, declared value excess profits taxes, and excess profits taxes. (R. 6.) The Tax Court upheld the exemption for 1941 but sustained the Commissioner's determination for 1942 and 1943. (R. 23.) Upon review the court below affirmed the decision of the Tax Court as to those years. (R. 155.)

ARGUMENT

There is no occasion for further review. The case turns on unique facts and no question of general importance is presented.

1. The case was correctly decided by the Tax Court and the court below. There is no dispute as to the findings of the Tax Court with respect to the Club's operations during 1942 and 1943 and there is no question but that its activities in those years were different from what they were in earlier years. The Tax Court found that the Club had definitely curtailed its operations in behalf of its members for the benefit of a wholly transient clientele and that the change produced profits entirely out of proportion to the income which principal operation for the members had produced (R. 25). These findings are fully supported by the evidence which shows that

during the years 1942 and 1943 any commissioned officer of the Armed Forces could use the Club at his own pleasure, the uniform being the only qualification for his admission. (R. 20.) Despite the admittedly laudable intention of the Club in affording its facilities to officer personnel, these persons were not members of the Club but were an unlimited number of a designated group of the general public insofar as the purpose of the organization was concerned, and only as a result of their use of its facilities were the income and profits of the Club so greatly increased. The Tax Court's final conclusions that the Club engaged in regular commercial acivities resulting in extraordinary profits (R. 21, 25, 154 and 155), and that this substantial business had only an indirect relation to the original purpose for which the Club was organized (R. 27 and 155) have a substantial basis in the evidence and are not open to review. *Dobson* v. *Commissioner,* 320 U. S. 489, rehearing denied, 321 U. S. 231.

In holding that a social club loses its exempt status if its operations are changed from normal club activities into commercial pursuits and that profits resulting therefrom inured to the benefit of the members whether distributed or not, the Tax Court followed principles laid down in the applicable regulations (Section 29.101 (9)–1 of Regulations 111, Appendix, p. 18, *infra*) and in other decided cases. See *Jockey Club* v. *Helver-*

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ing, 76 F. 2d 597 (C. C. A. 2d); *West Side Tennis Club* v. *Commissioner,* 111 F. 2d 6 (C. C. A. 2d), in which this Court denied certiorari, 311 U. S. 674.

The regulation in question denies exemption to a club which engages in traffic for profit. The same provisions were incorporated in Article 101 (9)–1 of Regulations 101, promulgated under the Revenue Act of 1938, and in Section 19.101 (9)–1 of Treasury Regulations 103, promulgated under the Internal Revenue Code.[2] The regulations, therefore, have received legislative approval and have the force and effect of law. *United States* v. *Safety Car Heating Co.,* 297 U. S. 88; *Hassett* v. *Welch,* 303 U. S. 303; *Helvering* v. *Winmill,* 305 U. S. 79, 83; *Boehm* v. *Commissioner,* 326 U. S. 287, 291–292, and compare *Better Business Bureau* v. *United States,* 326 U. S. 279.

The regulation is clearly in accord with the statute which requires not only that the Club be organized exclusively for pleasure, recreation and other non-profitable purposes, but also that it be operated exclusively for such purposes. It is

[2] Earlier regulations were similar except that they either did not contain any provision as to sales of property (see e. g., Article 530 of Regulations 77, promulgated under the Revenue Act of 1932), or provided that where the club sells any of its property at a profit it is not exempt for the year in which the profit is taxable. Article 101 (9)–1 of Regulations 86, promulgated under the Revenue Act of 1934.

therefore immaterial whether the Club's organization or its purposes changed since its operations did change. The fact that exemption exists for one year does not compel the conclusion that it exists for other years (cf. *Jockey Club* v. *Helvering, supra,* and *West Side Tennis Club* v. *Commissioner, supra*) where, despite the fact that the organization is still the same organization nominally, its activities are different.[3]

2. The Club asserts (Pet. 12, 13) probable conflict with the decision of this Court in *Trinidad* v. *Sagrada Orden,* 263 U. S. 578. It quotes a portion of the opinion to show that a quantitative test, which in the sense that petitioner uses the term was not in fact applied by either the Tax Court or the court below, is improper. However, the Club misplaces its reliance upon the statement in that opinion that not the source of income but its destination is the ultimate test of exemption. The statement was made only in connection with the determination of the exclusive operation of

[3] In this connection see Sections 29.101–1 and 29.101–2 of Treasury Regulations 111 relating to proof of exemption where operations change from year to year (Appendix, *infra*). Where a social club has no exemption status for a particular year, it is required to file a return as any other corporation under Section 52 of the Internal Revenue Code (Appendix, *infra*), or for part of a year under Section 29.52–1 of Treasury Regulations 111 (Appendix, *infra*). Moreover, every exempt corporation is required by Section 54 (f) of the Internal Revenue Code (Appendix, *infra*) to file a return for years beginning after December 31, 1942.

the corporation sole in that case for religious purposes. This Court pointed out that the income of the corporation from whatever sources could only be used for those purposes. The statement relied upon thus means only that if all of the income from incidental activities is used for the purposes for which exemption is granted its source is immaterial because the activities are incidental. Since in the instant case the operations of the Club in 1942 and 1943 were extraneous to and were not incidental to the purpose for which the Club was organized the source of the income and profits was material in deciding upon exemption and there is no conflict between the decisions here and that in the *Sagrada Orden* case.

For the same reason, there is no conflict with the decisions in *Santee Club* v. *White,* 87 F. 2d 5 (C. C. A. 1st); *Koon Kreek Klub* v. *Thomas,* 108 F. 2d 616 (C. C. A. 5th); *Coeur D'Alene Country Club* v. *Viley,* 64 F. Supp. 540 (D. Idaho). The income in those cases was from operations incidental to the normal and organizational purposes of the Club. Nor is there conflict with the decisions in *Roche's Beach, Inc.* v. *Commissioner,* 96 F. 2d 776 (C. C. A. 2d), and in *Debs Memorial Radio Fund* v. *Commissioner,* 148 F. 2d 948 (C. C. A. 2d). The statutory basis of the exemption granted in those cases is fundamentally different from the basis of exemption under Section 101 (9) (Appendix, *infra*). In the *Roche's Beach*

case, *supra,* exemption was allowed, under a provision equivalent to Section 101 (6) of the Internal Revenue Code, because the corporation was organized and operated exclusively for charitable purposes. In the *Debs Memorial Radio Fund* case the exemption was allowed, under Section 101 (8) of the Code, because the corporation was an organization not organized for profit and operated exclusively for the promotion of social welfare. In those cases we find the public purpose concept of exemption recognized in *Trinidad* v. *Sagrada Orden, supra.*

Moreover in those cases, as in the *Sagrada Orden* case and the others with which the Club here asserts conflict, the income was from incidental activities and could only be used for the specified organizational purposes. Neither the public purpose aspect of exemption nor the incidental activities feature are present in the instant case and the *Roche's Beach* and *Debs Memorial Radio Fund* cases, *supra,* are not in point in the consideration of exemption for social clubs.

This is clear since those cases were decided by the same court which had decided the *Jockey Club* and *West Side Tennis Club* cases, *supra,* and it apparently saw no conflict in its decisions of cases involving a public purpose with its decisions of cases involving social clubs. In *Sun-Herald Corp.* v. *Duggan,* 160 F. 2d 475, the Circuit Court of Appeals for the Second Circuit said that the

Roche's Beach case held only that the certificate of incorporation was not the only test of whether a corporation was "organized" for educational or other similar purposes under subdivision fourteen.

In the case of *Bohemian Gymnastic Ass'n Sokol of City of N. Y.* v. *Higgins,* 147 F. 2d 774 (C. C. A. 2d), involving the application of social security taxes to a corporation organized exclusively for educational purposes the same court said that if the *Bohemian Ass'n* were a social club its decisions in the *Jockey Club* and *West Side Tennis Club* cases might require it to hold that the receipt of such a large proportion of its income from a bar and restaurant patronized as they were not only by members, but even more by the outside public, the exact situation in the instant case, negatives tax exemption. In that decision the Circuit Court of Appeals pointed out the rationale of its position with respect to the exemption statutes as applied in other cases, which establishes the absence of any conflict between the decisions in the instant case and those in the *Roche's Beach* and the *Debs Memorial Fund* cases.

The case of *Scofield* v. *Corpus Christi Golf & Country Club,* 127 F. 2d 452 (C. C. A. 5th), presents a slightly different situation but there is no conflict of the decisions here with that decision. In that case the contention was made that the club was not exempt under Section 101 (9) of the Revenue Act of 1936, c. 690, 49 Stat. 1648, because

it derived profits from a continuing oil lease upon its property. There was, however, no discontinuance of the usual club operations for the exclusive benefit of its members and the majority of the court distinguished that case from the *West Side Tennis Club* and *Jockey Club* cases on the ground that the club was not engaged in the operations which produced the income. While that case may be said to extend the concept of "incidental" activities of a club to an extreme point the fact that there was no actual change in the operations of the club to produce unusual revenue, and that the club itself did not engage in the operations which produced that revenue are distinctions which are fatal to the assertion of a square conflict with the decisions below in the instant case necessitating review by this Court.

CONCLUSION

The decision below is correct. No question of great public importance is involved and there is no conflict of decisions. The petition should, therefore, be denied.

Respectfully submitted.

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APPENDIX

INTERNAL REVENUE CODE

SEC. 52. CORPORATION RETURNS.

(a) *Requirement.*—Every corporation subject to taxation under this chapter shall make a return, stating specifically the items of its gross income and the deductions and credits allowed by this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe. * * * (26 U. S. C. 1940 ed., Sec. 52.)

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SEC. 54. RECORDS AND SPECIAL RETURNS.

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(f) [as added by Sec. 117 of the Revenue Act of 1943, c. 63, 58 Stat. 21] Every organization, except as hereinafter provided, exempt from taxation under section 101 shall file an annual return, which shall contain or be verified by a written declaration that it is made under the penalties of perjury, stating specifically the items of gross income, receipts, and disbursements, and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner, with the approval of the Secretary, may by regulations prescribe, and shall keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Commissioner, with the

approval of the Secretary, may from time to time prescribe. * * *

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(26 U. S. C. 1940 ed., Sec. 54.)

SEC. 101. EXEMPTIONS FROM TAX ON CORPORATIONS.

The following organizations shall be exempt from taxation under this chapter—

* * * * *

(9) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder;

* * * * *

(26 U. S. C. 1940 ed., Sec. 101.)

REGULATIONS 111, PROMULGATED UNDER THE INTERNAL REVENUE CODE

SEC. 29.52–1. *Corporation Returns.*—Every corporation not expressly exempt from tax must make a return of income, regardless of the amount of its net income. In the case of ordinary corporations, the return shall be on Form 1120. * * * A corporation having an existence during any portion of a taxable year is required to make a return. * * *

* * * * *

SEC. 29.101–1 [as amended by T. D. 5381, 1944 Cum. Bull. 188]. *Proof of Exemption Prior to January 1, 1943—Annual Returns for Accounting Periods Beginning Prior to January 1, 1943.*—A corporation is not exempt merely because it is not organized and operated for profit. In order to establish its exemption it is necessary that every

organization claiming exemption file with the collector for the district in which is located the principal place of business or principal office of the organization an affidavit or a questionnaire as set forth below. An organization claiming exemption under section 101 * * * (9), * * * shall file the form of questionnaire appropriate to its activities, filled out in accordance with the instructions on the form or issued therewith. Copies of the following questionnaire forms may be obtained from any collector: For corporations claiming exemption under section * * * 101 (9), Form 1025; * * * An organization claiming exemption under section 101 * * * (9) * * * shall also file with the other information specified herein a return of information on Form 990 relative to the business of the organization for the last complete year of operation; * * *

The words "private shareholder or individual" in section 101 refer to individuals having a personal and private interest in the activities of the corporation. * * *

* * * * *

When an organization * * * has established its right to exemption, it need not thereafter make a return of income or any further showing with respect to its status under the law, unless it changes the character of its organization or operations or the purpose for which it was originally created, except that every organization exempt or claiming exemption under section 101 * * * (9) * * * shall file annually returns of information on Form 990 with the collector for the district in which is located the

principal place of business or principal office of the organization; * * *

* * * * *

SEC. 29.101 (9)–1. *Social Clubs.*—The exemption granted by section 101 (9) applies to practically all social and recreation clubs which are supported by membership fees, dues, and assessments. If a club engages in traffic, in agriculture or horticulture, or in the sale of real estate, timber, etc., for profit, such club is not organized and operated exclusively for pleasure, recreation, or social purposes. Generally, an incidental sale of property will not deprive the club of the exemption.

SEC. 29.101–2 [as added by T. D. 5381, 1944 Cum. Bull. 188]. *Proof of Exemption on or After January 1, 1943—Annual Returns for Accounting Periods Beginning on or After January 1, 1943.*—(*a*) *Proof of exemption.*—An organization is not exempt from tax merely because it is not organized and operated for profit. In order to establish exemption it is necessary that every organization claiming exemption file with the collector for the district in which is located the principal place of business or principal office of the organization an affidavit or questionnaire as set forth below. An organization claiming exemption under section 101 * * * (9) * * * shall file the form of affidavit or questionnaire appropriate to its activities, filled out in accordance with the instructions on the form or issued therewith. Copies of the following forms may be obtained from any collector: For organizations claiming exemption * * * under section 101 (9), Form 1025; * * *

* * * * *

(*d*) *"Private shareholder or individual" defined.*—The words "private shareholder or individual" in section 101 refer to persons having a personal and private interest in the activities of the organization.

(*e*) *Requirement of annual returns.*—For accounting periods beginning after December 31, 1942, every organization exempt from tax under section 101, regardless of the amount or source of its income or receipts * * * shall file annually with the collector * * * a return of information on Form 990 (revised May, 1944) specifically stating the items of gross income, receipts, and disbursements and such other information as may be prescribed by the Commissioner * * *.

* * * * *

(*j*) *Records, statements, and other returns of tax-exempt organizations.*—An organization which has established its right to exemption from tax under section 101 * * * shall immediately notify in writing the collector for the district in which is located its principal office of any changes in its character, operations, or purpose for which it was originally created.

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